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Armand L. Smith and Virginia L. Smith v. Fairfax Realty, Inc. (formerly Price Development Company), North Plains Land Company, LTD., and North Plains Development Company, LTD. : Reply Brief

Utah Supreme Court

Harold G. Christensen; Reed L. Martineau; Rex E. Madsen; Snow Christensen & Martineau; James S. Jardine; Brent D. Wride; Rick B. Hoggard; Rod N. Andreason; Ray Quinney & Nebeker; Attorneys for Defendants/ Appellants.
Robert S. Campbell; Clark K. Taylor; Van Cott Bagley Cornwall & McCarthy; Attorneys for Plaintiffs/Appellees.

IN THE UTAH SUPREME COURT

ARMAND L. SMITH and VIRGINIA L. SMITH,

Plaintiffs/Appellees,

vs.

FAIRFAX REALTY, INC. (formerly PRICE DEVELOPMENT COMPANY), NORTH PLAINS LAND COMPANY, LTD., and NORTH PLAINS DEVELOPMENT COMPANY, LTD.,

Defendants/Appellants.

REPLY BRIEF OF APPELLANTS

Case No. 20010673-SC

APPEAL FROM THE JUDGMENT OF THE THIRD JUDICIAL DISTRICT COURT, HONORABLE FRANK G. NOEL PRESIDING, SALT LAKE CITY, STATE OF UTAH

Robert S. Campbell, Jr.
Clark K. Taylor
VAN COTT, BAGLEY, CORNWALL & McCARTHY
50 South Main, Suite 1600
Post Office Box 45340
Salt Lake City, Utah 84145-5340

Attorneys for Appellees

Harold G. Christensen
Reed L. Martineau
Rex E. Madsen
SNOW, CHRISTENSEN & MARTINEAU
10 Exchange Place, Eleventh Floor
Post Office Box 45000
Salt Lake City, Utah 84145-5000

James S. Jardine
Brent D. Wride
Rick B. Hoggard
Rod N. Andreason
RAY, QUINNEY & NEBEKER
36 South State Street, Suite 1400
P.O. Box 45385
Salt Lake City, Utah 84145-0385

Attorneys for Appellants

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50 South Main, Suite 1600
Post Office Box 45340
Salt Lake City, Utah 84145-5340

Attorneys for Appellees

Harold G. Christensen
Reed L. Martineau
Rex E. Madsen
SNOW, CHRISTENSEN & MARTINEAU
10 Exchange Place, Eleventh Floor
Post Office Box 45000
Salt Lake City, Utah 84145-5000

James S. Jardine
Brent D. Wride
Rick B. Hoggard
Rod N. Andreason
RAY, QUINNEY & NEBEKER
36 South State Street, Suite 1400
P.O. Box 45385
Salt Lake City, Utah 84145-0385

Attorneys for Appellants

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INTRODUCTION

Stripped of the rhetoric, this case turns on two key questions: (1) was there a reasonable probability that Fairfax could have sold or refinanced the Mall for $16 million prior to the July 1994 expiration of the Chemical Bank loan, and, if so, (2) was Fairfax's determination that the REIT was the only reasonable alternative to foreclosure so reckless or malicious as to justify, not only an award of punitive damages, but an award that is presumptively excessive under Utah law. Applying the relevant standards of review to these questions requires a negative answer to both.

First, even with the deferential standard of review following the jury's verdict in favor of the Smiths, as a matter of law, the Smiths failed to meet their burden of proof on liability with respect to causation.[1] It is undisputed that Chemical Bank sent a notice of default on the loan in July 1993 and, if not for the REIT, it would not have extended the loan. The Smiths point to no contrary evidence. On the issue of whether there was any alternative to avoid foreclosure other than the REIT, the Smiths' sole evidence was the testimony of their appraiser, Howden, that as of January 1, 1994, he thought the Mall property could be sold for $16 million if left on the market for one year. But since a year was not available to the Partnerships, Howden's testimony is not evidence of a reasonable probability that a sale would have occurred before foreclosure. Without a showing of a

[1] The Smiths erroneously contend that Fairfax has not appealed the sufficiency of the evidence on liability. Fairfax has clearly raised (what the Smiths call) the "'bankruptcy or REIT' defense" as to both compensatory and punitive liability on appeal. (Fairfax Br. at 25-28, 30-34; see also id. at 25-26 n.34 ("If the REIT was the only available alternative, then the Smiths' claims would fail on several related grounds," including causation, proof of damages, and breach of duty.)

reasonable alternative to save the Mall, as a matter of law, the Smiths cannot establish that Fairfax's conduct proximately caused any damage.

Second, there was insufficient evidence to submit punitive damages to the jury, much less to support a presumptively excessive award. This Court reviews punitive damages de novo, both for due process issues as well as under the Crookston I factors. A de novo review of the entire record reveals no basis for a finding of malice. Because the standard of review is de novo, the Smiths' brief should have addressed the entire record. Instead it largely ignores the evidence in the record against punitive damages. Significantly, neither the Smiths' brief nor the District Court's findings even addresses Fairfax's belief (right or wrong) that the REIT was the only viable alternative. In addition, the Smiths spend much of their brief emphasizing conduct that is clearly unrelated to the REIT decision and for which they assert no injury or damages, e.g., combining Partnership accounts, accruing (but never paying) interest on Fairfax's capital call contribution, following the advice of Fairfax's tax accountant on tax allocations to the partners, and John Price's profits from the contribution of over seventy other unrelated properties to the REIT. Such conduct, even if correctly described by the Smiths (which it is not), is not relevant to liability or the damages in this case.

Third, the District Court erred in allowing the jury to award prejudgment interest as "damages," contrary to almost a century of Utah precedent. The jury's excessive award of interest in this case demonstrates the wisdom of that precedent.

REPLY ARGUMENTS[2]

I. BECAUSE FAIRFAX'S REIT DECISION WAS THE ONLY REASONABLE ALTERNATIVE TO AVOID FORECLOSURE, FAIRFAX'S ACTIONS DID NOT CAUSE THE SMITHS ANY INJURY.

A. Preservation of Issue for Appeal.

The Smiths argue that Fairfax did not raise "causation" at trial. (Smiths' Br. at 46.) To the contrary, Fairfax repeatedly argued below that (what the Smiths call) its "bankruptcy or REIT" defense limited possible damages to REIT value (which the Smiths did not contest), rather than appraised fair market value. This is the very causation issue raised here on appeal.[3]

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[2] The Smiths make the shopworn argument that Fairfax failed to marshal the facts, notwithstanding the twenty pages devoted to the facts in Fairfax's brief. (Smiths' Br. at 2, 26-28.) But the Smiths do not identify any specific material "fact" that Fairfax omitted. Instead, the Smiths identify only two omitted "core issues" (the "consent" and "valuation" issues) (Smiths' Br. at 3, 12), both of which were in fact described by Fairfax. (Fairfax Br. at 10 n.5, 14 n.21, 15 n.23.) The Smiths also assert that Fairfax "phrased deceptively" and insincere[ly]" the evidence. (Smiths' Br. at 26, n.6.) However, the examples cited by the Smiths show that Fairfax was characterizing disputed evidence at trial but properly setting forth the Smiths' version of the facts.

[3] Fairfax unsuccessfully moved for summary judgment (and in limine) on damages, arguing that the REIT was the only available alternative to avoid a "total loss" of the Mall, which limited damages to a REIT valuation rather than an appraised valuation. (See, e.g., R 3117-18 ("If the jury concludes that the property was sold for a proper value under REIT practices and standards, then the [Smiths] were not damaged"); 3130 ("The question of damage must be considered in light of the fact that the REIT was the only available alternative to avoid a total loss of the property"); see also R 1729, 1733-34, 1737-38, 1927, 3755, 3756, 3762, 4538 at 7, 10, 56.) During trial, Fairfax made the same argument on directed verdict (R 4545 at 1003; R 4550 at 2034), in opposition to the Smiths' motion as to the measure of damages (R 4546 at 1197), and in objection to the jury instruction that took REIT valuation from the jury (R 4551 at 2132, 2138, 2141-42). After trial, Fairfax moved for judgment or a new trial, again arguing that the REIT was the only way "to avoid total loss," which should have limited the Smiths' measure of damages, if any, to REIT valuation (R 3755-56, 3759, 3762-64, 3807-10).

B. Causation and Damages Require Proof of a Reasonable Probability or Certainty that the Smiths Could Have Sold the Mall for Full Value Prior to July 1994.

In its initial brief, Fairfax argued that, as a matter of law, the Smiths had the burden to show a "reasonable probabilit[y]" of selling the Mall for $16 million prior to foreclosure to establish proximate causation under Mahmood v. Ross, 1999 UT 104, ¶38, 990 P.2d 933. In response, the Smiths argue that Mahmood dealt with "consequential" rather than "general" damages. That distinction, however, is immaterial because proof of proximate causation is required for both general and consequential damages. Indeed, Mahmood derived its standard from general causation principles. Id., at ¶22 (quoting Sumsion v. Streator-Smith, Inc., 132 P.2d 680, 683 (Utah 1943)); see also Highland Constr. Co. v. Union Pac. RR. Co., 683 P.2d 1042 (Utah 1984) ("whether general or special, damages must be traceable to the wrongs complained of").

The Smiths also argue that Fairfax confuses "injury" with "damage." (Smiths' Br. at 48-49.) But the injury/damage distinction urged by the Smiths is also immaterial because, even under a damages analysis, the Smiths must still establish the "fact of damage" with a "reasonable certainty" or "probability." See Mahmood, 1999 UT 104, ¶20; see also Sawyers v. FMA Leasing Co., 722 P.2d 773, 774 (Utah 1986) ("fact of damages must be proven with reasonable certainty"); Atkin Wright & Miles v. Mountain State Tel. & Tel. Co., 709 P.2d 330, 336 (Utah 1985) ("The evidence must . . . give rise to a reasonable probability that the plaintiff suffered damage as a result of the breach").

C. The Smiths Did Not Prove that There Was a Reasonable Probability or Certainty of Any Recovery But for the REIT.

The key causation issue at trial, on which the Smiths had the burden of proof, was whether there was any reasonable alternative to avoid foreclosure other than the REIT. The Smiths claim that the Mall was not "headed toward foreclosure" because of the Mall's good occupancy and financial performance. (Smiths' Br., ¶ 3 at 5-6.) The Smiths miss the point—the Mall faced foreclosure and bankruptcy not due to low tenancy or poor performance but because of the undisputed impending loan default unless either extended, refinanced, or paid by sale of the Mall. There was no reasonable prospect of such extension, refinancing, or sale prior to default.

1. Fairfax Could Not Extend or Refinance the Chemical Bank Loan.

The evidence showed that Chemical Bank would not have extended the loan for a seventh time beyond July 1994. Indeed, it was undisputed that Chemical Bank (1) issued a notice of default in July 1993,[4] (2) granted the sixth extension solely to complete the REIT, (3) refused additional extensions, and (4) changed its internal policies to "get [loans] off the books" because the financing market had "evaporated." (Fairfax Br. at 8 n.13.)

The Smiths offered no evidence that the Partnerships could have refinanced the Mall prior to July 1994. The undisputed evidence was that Fairfax had used two national brokers to attempt to refinance the Mall since 1988 (with only one offer to refinance at one-half the loan balance) and was told by its second broker that he had "exhausted" his efforts and "it would be very difficult" to refinance any amount over $9 million, let alone the $12 million needed.[5] (Smiths' Br., ¶ 5 at 7; see also Fairfax Br. at 6-7, n.12.)

2. Fairfax Made Extensive Efforts to Sell the Mall.

In addition to the refinancing efforts, it was undisputed that Fairfax also had unsuccessfully tried to sell the Mall for years.[6] (Fairfax Br. at 7.) Fairfax's broker testified that by 1993 he had "exhausted all the avenues and there was basically no one interested in buying the property." (Id. n.12 (quoting R 4548 at 1603-05).) Nevertheless, Fairfax continued its own efforts (including asking the Smiths to find a buyer)[7] until the REIT closed. (R 4550 at 1914, 1929.) The Smiths concede they were told in December

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[4] The Smiths state that the loan was not in "default" on September 23, 1993, the date of the last extension. (Smiths' Br. at 6.) However, that fact means nothing since by that date Chemical Bank had agreed to one last extension to complete the REIT.

[5] The Smiths erroneously claim Mr. Oliver's refinancing attempts were "[i]nvariably" a "package deal" with other malls. (Smiths' Br., ¶ 5 at 7.) In fact, Oliver said he initially packaged the Mall with "better" properties to improve the Mall's chances (R 4548 at 1595-96, 1598), but he also tried to market the Mall "by itself" (id. at 1599).

[6] The Smiths claim Mr. Oliver "was not even retained to find a potential buyer," but the Smiths omit key portions of Mr. Oliver's testimony. (Smiths' Br. at 7.) He actually said "[w]hen we were *first* retained, the objective was to . . . to refinance the loan . . . . *But the agreement was left open and there was an understanding to look for other alternatives. As we saw that financing was very difficult . . . we also looked at other alternatives such as . . . selling the property.*" (R 4548 at 1615) (emphasis added).)

[7] The Smiths argue that Fairfax's request for their help occurred in December 1993, but "astonishing[ly] . . . did not disclose . . . that the Mall had already been contributed to the REIT." (Smiths' Br. at 37.) The Smiths are wrong. The December 1993 letter clearly stated that Fairfax's request for the Smiths' help had been made "some time ago." (Fairfax Br. at 13 (quoting P-65).) Moreover, although the Contribution Agreement was signed prior to December 1993, it was conditioned on the REIT closing, so that the Mall had not yet been conveyed to the REIT. (Id. at 11 (citing P-58, P-59).)

1993 that Fairfax's efforts to sell or refinance had failed. (Smiths' Br. at 45; Fairfax Br. at 13 (quoting P-65).)

3. The Smiths Submitted No Evidence that the Mall Could Have Been Sold Prior to Foreclosure.

There was no evidence presented to the jury from which it could have found that the Mall could have been sold for $16 million prior to the foreclosure date. The Smiths' only evidence on this point was the testimony of an appraiser (Howden) that "a willing buyer would have paid $16,000,000 for the [Mall] as of January 1, 1994." (Smiths' Br., ¶ 7 at 8.) But Howden himself did not testify that the Mall could have been sold for $16 million under the actual circumstances faced by Fairfax. Indeed, Howden expressly premised his opinion on the condition that the Mall "remained on the market in 1994 for a period of approximately one year" where Fairfax was not "compelled" to sell. (R 4543 at 673; see also Smiths' Br. at 47-48.) The undisputed evidence, however, shows that the Mall could not have remained on the market for a year. By July 1993 Fairfax had already received a notice of default, which (even with the full extension) would have expired in half that time. In fact, in the absence of the REIT, the Partnerships were already in the position of being compelled by Chemical Bank to sell as of January 1994—the date of Howden's valuation. In any event, even if Howden had testified that the Mall could have been sold before July 1994 (which he did not), his opinion would have been sheer speculation because he was uninformed about the history of prior unsuccessful attempts to refinance or sell the Mall.[8] (R 4543 at 670-74.)

The Smiths did not prove a reasonable probability or certainty (for proximate cause and damages purposes) that the Mall could have been sold for $16 million (or even at all) by July 1994 if it had not been contributed to the REIT. In Mahmood, this Court rejected causation as speculative as a matter of law where there was no evidence of any actual attempt to refinance property prior to foreclosure. Mahmood, 1999 UT, ¶ 28. In the present case, Fairfax exhausted its efforts to sell or refinance the Mall, the Smiths never responded to Fairfax's request that they find a buyer, and the Smiths did not contest the reasonableness of Fairfax's efforts. Under these circumstances, the "probabilities" that the Mall would not have been sold for $16 million before July 1994 are "equally or more potent" than the probabilities that it would be so sold. Thus, the Smiths' "deductions are mere guesses and the jury should not [have] be[en] permitted to speculate."[9] Id., ¶ 22. The District Court thus erred in denying Fairfax's "bankruptcy or REIT" defense.

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[8] Howden in fact testified that, given the market, he believed the "Mall [could have] obtained a long-term financing commitment or . . . loan in the early 1990s" (Fairfax Br. at 7 nn. 10, 12 (citing R 4543 at 672; 4548 at 1604)), the very time when a national broker had unsuccessfully but exhaustively attempted to refinance the Mall. Howden and the Smiths made no attempt to question these actual efforts.

[9] The Smiths call Fairfax's argument that it had no option other than the REIT to avoid foreclosure an "absolute falsehood." (Smiths' Br. at 41 n.11.) In addition to speculating that the Mall could have been sold, the Smiths claim that Fairfax should have obtained their consent. The Smiths also suggest that Fairfax could have waited until July 1994 to make its decision. Moreover, inasmuch as the Mall could not have formed its own REIT (R 4545 at 1123-24), Fairfax had to make the decision in January 1994 of how to proceed. However, if the Smiths would have given their consent, then the Smiths suffered no damages. If the Smiths would have refused consent, then the Mall would have been lost to foreclosure, so again they prove no damages.

II. THE DISTRICT COURT ERRED ON PUNITIVE DAMAGES.

The District Court erred in its rulings on punitive damages in several ways. First, the District Court should not have permitted the issue of punitive damages to go to the jury. Second, even if it correctly allowed punitive damages to go to the jury, the District Court committed clear error in permitting the jury to include prejudgment interest in compensatory damages and in failing to analyze or reduce the excessiveness of the punitive damages award under the Crookston I factors. These errors should be corrected by this Court under its de novo review of the punitive damage award.

A. De Novo Review of the Punitive Damage Award Is Required.

The Smiths argue that Fairfax made no due process challenge to punitive damages, precluding de novo review. (Smiths' Br. at 23, 29-33.) To the contrary, Fairfax has challenged the constitutionality of the punitive damages.[10] (Fairfax Br. at 45 n.39 ("The same conclusion is directed by federal law[] [u]nder the three guideposts for federal due process analysis"); see also id. at 2, 35, 36-37 (citing federal due process cases); id. at 36 n.35, 39, 44 (invoking "due process" or "constitutional" principles).) In any event, this Court clearly "adopt[ed] the de novo standard for reviewing jury and trial court conclusions under the Crookston I factors," even when evaluating non-constitutional

[10] The Smiths make much of Fairfax's failure to set out the text of the due process clause on page three of its brief. (Smiths' Br. at 29.) Fairfax did not quote the text of the due process clause in the introductory portion of its brief because "interpretation" of the constitutional text is not at issue in this case, as opposed to the relevant case law thereunder (such as Campbell). Moreover, as the Smiths concede, it is the argument rather than the preliminary sections in a brief that determines whether an issue has been raised. (Smiths' Br. at 30 n.7 (citing Campbell v. State Farm Mut. Ins. Co., 2001 UT 89, n.8).)

challenges. Campbell v. State Farm Mutual Auto. Ins. Co., 2001 UT 89, ¶13, Utah Adv. Rep. 44, cert. granted, 122 S. Ct. 2326 (2001); see also id., ¶¶ 15, 22.[11]

B. There Was No Evidence Justifying any Award of Punitive Damages.

Regardless of the standard of review, there was no evidence of any conduct that would justify the submission of the issue of punitive damages to the jury. Fairfax actually and reasonably believed the REIT to have been the only alternative to foreclosure, and Fairfax further relied on outside legal and financial advisors throughout the REIT process, so that Fairfax did not act recklessly or with malice.

1. Fairfax Believed It Had No Alternative to the REIT.

Even if the Smiths were correct that a buyer would have materialized somehow in early 1994, it was undisputed that Fairfax actually believed that to avoid foreclosure there was no alternative to the REIT. (R 4545 at 1088-89, 1097, 1235; 4550 at 1923.) Fairfax's belief (right or wrong) was reasonable because it had tried to refinance or sell the Mall for nearly five years using its own contacts and two national brokers. It was told by the second broker that he had "exhausted" his efforts with no one interested (despite his every motive to successfully market the Mall to earn a commission). (R 4548 at 1603-04.) Fairfax so informed the Smiths, who failed to propose any reasonable

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[11] In Campbell, this Court separately evaluated the punitive damages under federal due process standards and under state law, but still used de novo review for the state-law challenge, which was under Crookston I rather than the Utah Constitution. Id. at n.8 (Court did not consider the Utah Constitution). In addition, this Court has always reviewed the seventh Crookston I factor (ratio of damages) for "correctness." Id. at ¶ 13.

alternative to the REIT. The Smiths' brief (and the District Court's findings) are inexplicably silent on this key issue of Fairfax's intent.

2. Fairfax Did Not Contribute the Mall to the REIT for any Allegedly Improper Benefit for Itself.

The Smiths repeatedly argue that the "real reason" the Mall was contributed to the REIT was for John Price's personal benefit. (Smiths' Br., ¶¶ 6, 15 at 7-8, 15-16, 24, 33, 36, 40, 42.) But the Smiths' argument is negated by two undisputed facts:

- Fairfax could have gone ahead with the REIT for the over seventy other properties without the Mall—although to the detriment of the Partnerships.
- Price would have received the same personal benefits (or even more) from the REIT if the Mall had not been contributed to the REIT.

(Fairfax Br. at 9 n.14.) Since the REIT could have proceeded without the Mall and since Price would have received essentially the same (if not greater) benefit if the Mall had not been contributed to the REIT, Fairfax's decision to contribute the Mall to the REIT could not have been influenced by any non-Partnership benefits to Price—there were no additional personal benefits for him to receive.[12] It was undisputed that the Partnership benefits were shared proportionately with (and in fact disproportionately in favor of) the Smiths. The District Court's findings did not attribute the REIT decision to alleged self-

[12] The Smiths suggest that Fairfax did not want to sell the Mall because of "major adverse tax consequences" of a sale due to Price's negative capital account in the Partnerships. (Smiths' Br. at 7, 10, 15, 36, 40.) However, aside from the fact that the REIT also avoided similar tax problems for themselves as well, the Smiths simply do not respond to the undisputed evidence at trial that "such a sale probably would not have resulted in the mentioned tax consequences," or that such tax consequences were not in fact "considerations" during the attempted sale of the Mall. (Fairfax Br. at 6 n.9 (citing R 4550 at 1989, 2012).)

interest, and the evidence fails to support the Smiths' characterization of Fairfax's alleged motives. Price's personal benefit from contribution of numerous non-Partnership properties to the REIT is simply irrelevant to this case.

3. Fairfax Relied on the Advice of Counsel in the REIT Process.

The Smiths assert as "core" issues that their consent to the REIT was required and that the Mall had to be appraised. (Smiths' Br. at 3, 12.) Yet there is no dispute that Fairfax was advised by competent legal counsel and REIT experts on the consent, valuation, and disclosure issues. (Fairfax Br. at 9-11 (citations).) Whether or not the advice obtained by Fairfax was correct, in relying on that advice Fairfax did not act maliciously or wrongfully. (Fairfax Br. at 29 (citing, inter alia, Calhoun v. Universal Credit Co., 146 P.2d 284, 288 (Utah 1944) (honest belief that conduct was lawful precludes punitive damages even if belief was mistaken)).) The Smiths' assertion (without citation) that advice of counsel is "irrelevant" (id. at 38) is contrary to Utah law.

The Smiths argue (without any citation to the record) that Fairfax's reliance on advice of counsel lacks "foundation" (whatever that means) and allegedly did not address Fairfax's duties to the Smiths as a general partner. (Smiths' Br., ¶18 at 18, 25, 33, 38.) The Smiths are wrong. The record specifically discloses that Fairfax was advised by counsel that it could not discuss REIT specifics with the Smiths prior to that time because Mrs. Smith was an "unaccredited" investor under securities laws, that counsel evaluated the Partnership Agreements in advising Fairfax on whether consent was required, and, more importantly, that Fairfax was relying on these experts to advise it on how to discharge its fiduciary duties in this case. (R 4542 at 521; 4545 at 1084-86, 1103-05, 1114-15; 4550 at 1920, 1995-97.)

The District Court's findings fail to acknowledge that Fairfax obtained and relied on legal advice on the "core" issues.

4. Fairfax's January 1994 Disclosure of the Prospectus to the Smiths Contradicts the Smiths' Claims of Concealment for Fear of a Lawsuit.

The Smiths assert that Fairfax did not disclose information about the REIT prior to its closing and that the District Court found "a substantial reason for the non-disclosure was that Price 'did not want the Smiths to interfere by filing an adverse claim or potential lawsuit prior to [the REIT closing on] January 21, 1994.'" (Smiths' Br. at 19 (quoting R 4495).) Not only was there was no evidence in the record to support this finding, the undisputed evidence contradicts the Smiths' assertion. (Fairfax Br. at 13-14, nn.19-20.) The Smiths concede that Fairfax overnighted the REIT Prospectus to the Smiths on January 13, 1994.[13] (Smiths' Br. at 14.) Yet, the Prospectus disclosed virtually all of the facts that Fairfax was allegedly keeping "secret" from the Smiths—including the contribution of all of the Mall to the REIT, the method of valuation, the alleged "conflicts

[13] There is evidence in the record, consisting of Smith's own testimony, that he actually saw a "prospectus" as early as November/December 1993. (R 4540 at 295 (Smith told Mendenhall on December 2, 1993, that "[h]ere you organized a REIT, and part of the purpose, as I understand it from the prospectus, was you were going to raise some money to buy out [Cottonwood Mall] Partners") (discussing Exhibit 66, emphasis added).) In any event, the Smiths cannot deny that they knew the REIT would in fact go forward with the Mall prior to the REIT's closing—Smith received a personal guaranty of the new debt and was told to sign it by the time of the REIT closing on January 21, 1994, which Smith did. (Exs. 72, 74, 75.)

of interest," and John Price's benefit from the REIT.[14] (P-71 at 3, 44-45, 90.) Thus, one week prior to the REIT closing, the Smiths had all relevant information about the REIT, including (contrary to their assertion and the District Court's findings) the agreed contribution of the Mall to the REIT. If Fairfax had been allegedly motivated to conceal facts to avoid a lawsuit prior to January 21, 1994, it would not have sent the Prospectus to the Smiths prior to the REIT closing. Neither the Smiths' brief nor the District Court's findings acknowledges the impact of Fairfax's disclosure of the Prospectus to the Smiths on their allegations and findings of nondisclosure.

5. Fairfax Did Not Misallocate Tax Losses.

The Smiths assert—without any supporting evidence—that the allocation of Partnership losses for tax purposes was "deceitful and dishonest misconduct." (Smiths' Br. at 9, 24, 36.) However, it was undisputed that the losses were allocated by an outside accountant to comply with changes in the tax laws in 1991. (R 4547 at 1537-39, 1552-56, 1576, 1580.) Indeed, the District Court rejected the Smiths' argument on this point and struck this allegation from its findings—a fact the Smiths do not mention. (R 4510 (ruling); R 4394; Fairfax Br. at 21 n.32.)

6. Fairfax Did Not "Cook Its Books."

a. The Partnership Books Were Not Cooked.

The Smiths also contend that Fairfax "cooked the Partnership books." (Smiths'

[14] Ironically, while ignoring the facts disclosed in the Prospectus, the Smiths nevertheless repeatedly rely on the Prospectus to prove Fairfax's alleged self-dealing. (Smiths' Br. at 12, 14-16.)

Br. at 16, 24, 39-40, 43, 47.) However, it is unclear what the Smiths mean by that pejorative phrase because even the Smiths' own expert, Merrill Norman, made no such claim after his thorough review of the Partnership books. (See also R 4548 at 1667, 1725 (fraud examiner found no evidence of "cooked books").)

b. The March 1994 Letter Was Not Malicious.

The Smiths use the phrase "cooked books" to characterize the March 8, 1994 letter as "intentionally deceitful, dishonest," "bogus" and a "malicious . . . attempt . . . to intimidate and coerce" the Smiths. (Smiths' Br., ¶ 16 at 16, 24, 39, 41; Special Findings at R 4494-95 (bullet points 5, 7-8).) The Smiths assert that this letter is their "most important[]" punitive damages evidence on appeal. (Smiths' Br. at 24; see also Fairfax Br. at 17 n.25.) That assertion reveals the frailty of their punitive damages claim.

There is no question that (as with almost any calculation) the various REIT computations (December 1993, January 1994, and the two in March 1994) can be confusing. (Fairfax Br. at 16 n.24, 17 n.26.) Notwithstanding the potential confusion, the March 1994 letter does not support (but actually negates) a finding of malice by Fairfax. It was undisputed that a strict REIT valuation (using the methodology disclosed to the Smiths in December 1993) would have resulted in an allocation to the Smiths of 1,319 shares worth \$23,000. However, Price personally contributed an additional 12,000 shares to the Partnerships at the REIT closing (more than doubling the Partnerships' shares). The Smiths argue that an accurate accounting would have disclosed that Price's contribution would have increased their 15% interest to 3,119 shares, worth \$55,000. (Smiths' Br. at 16-17 ("Undisclosed by Price at the time was the fact that . . . [the]

Smiths' 15% interest was . . . $54,582.50"); Fairfax Br. at 12-13, 16 n.24.) However, the Smiths concede that Fairfax told them in January 1994 that their allocation was 13,319 shares (worth $233,000) and the March 1994 letter disclosed two computations of even higher value (between $236,000 and $254,000), which included the immediate, . preferential repayment of their capital call.[15] The Smiths misleadingly focus on one component of the calculation (the 352 shares in the shares/cash offer) to the exclusion of the fact that the total value of the offer was almost five times higher than what the Smiths claim was their entitlement—and more than all of the Partnerships' original allocation under a strict REIT accounting. While Fairfax obviously could have communicated more clearly in its attempt to resolve the Smiths' concerns, it is undisputed that Fairfax tried to favor the Smiths preferentially to its own disadvantage. This letter, which was sent after the REIT decision and merely explained its consequences, does not show malice, but rather that, as the REIT expert testified, Price went "overboard" to benefit the Smiths. (Fairfax Br. at 17.)

c. The Other Accounting Issues Raised by the Smiths Involve No Damage and Do Not Show Malice.

The Smiths raise other accounting issues to in an attempt to demonstrate Fairfax's alleged malice, but, significantly, they do not ever claim damages therefor. The Smiths charge that Fairfax's use of a single bank account was a "brazen and reckless breach[] of its fiduciary trust," justifying punitive damages. (Smiths' Br. at 8-9, 24, 35.) But Fairfax

[15] The offer was "preferential" to the Smiths because it would be paid ahead of Fairfax's capital call.

told the Smiths of this practice in 1991 (to which they raised no objection), and the testimony was that the practice benefited the Partnerships. (Fairfax Br. at 19, 33-34). Next, the Smiths assert that Fairfax made "secret" loans to the Partnerships. (Smiths' Br. at 24, 36.) This contention ignores the undisputed fact that it was Fairfax that told Smith about the loans (and the treatment of interest thereon). (Fairfax Br. at 6 n.8.) Finally, the Smiths assert that the payment of a 5% rather than 3.9% management fee was "dishonest." (Smiths' Br. at 9, 24, 36, 43.) However, since the Partnership Agreements provided that the management fee could be either 3.9 or 5.0 % depending on the circumstances, if it was a mistake, it was on its face an honest mistake. (Fairfax Br. at 19.) In any event, in December 1993 Fairfax provided the Smiths with audited financial information that clearly disclosed the management fee it had charged in 1990 through 1992, thereby negating any allegation that Fairfax was trying to hide its fees. (Ex. 65 at 2.) Consequently, these accounting practices (whether right or wrong) do not show malice or nondisclosure for the purposes of punitive damages.

7. Mr. Price's Testimony Was Not Relevant to Punitive Damages.

The Smiths strenuously argue that the individual testimony of John Price was the "hallmark" of the trial, "a bright line" supporting punitive damages that demonstrated "arrogance, pomposity and indifference" because Mr. Price could not answer Mr. Campbell's questions. (Smiths' Br. at 19-20, 42.) However, this examination of Mr. Price demonstrates no malice on the part of Fairfax and does not support punitive damages. The general partner and defendant was Fairfax, not John Price, who had only "minimal involvement" with the Partnerships. The responsible Fairfax employees

(Frazier and Mendenhall) in fact specifically answered the questions during the trial. (R 4542 at 568-73, 584, 589, 590, 593-96, 598-601, 609-10.) If Price's testimony is the "bright-line" of punitive damages, then the Smiths' right to punitive damages is extremely dim. The analytical clarity of de novo review by this Court should reject this argument for what it was—an irrelevant means to inflame the jury.

C. The Jury's Award of Punitive Damages Was Excessive under the Crookston I Factors.

In this case, judgment was entered for $7,124,744.60 (the bulk of which was punitive damages) on a dispute over whether the Smiths' Partnership interest should have been valued at $410,000 (as found by the jury) or at between $230,000 and $255,000 (as offered by Fairfax under the REIT in early 1994). Although the judgment was entered on Special Findings asserting that the punitive damages were "within the zone of reasonableness" (R 4497), there was no "detailed and reasoned articulation" as to why this case was "unique" so as to justify a presumptively excessive punitive damage award,[16] see Campbell 2001 UT 89, ¶¶ 15, 19. A de novo (or any other) review of the seven factors announced by this Court in Crookston I demonstrates that the award of punitive damages should be reversed or substantially reduced below the 3:1 guideline established by this Court.

[16] The Special Findings (which were drafted by the Smiths and adopted almost unchanged by the District Court) focused almost exclusively on Fairfax's alleged malice.

1. Fairfax's Relative Wealth

In response to Fairfax's specific arguments on wealth analyses in other cases, the Smiths simply assert that Fairfax[17] was wealthy (Smiths' Br. at 35), but make no attempt to address Fairfax's net worth relative to the size of the punitive damages award. The Smiths do not dispute that the punitive damage award in this case represented approximately 15% of Fairfax's total wealth. By contrast the punitive damage awards in Campbell and Crookston represented well less than 1% of the total wealth of those defendants. There is simply no basis in this case for awarding punitive damages in a relative amount that is over fifteen times higher than the amount awarded in Campbell.

2 - 3. The Nature of Fairfax's Conduct and The Facts and Circumstances Surrounding Fairfax's Conduct

In addressing these two factors, the Smiths substitute adjectives for analysis, listing numerous examples of what they allege to be "sordid" and "reprehensible" conduct. Each of the Smiths' specific conduct allegations is addressed above. As to the central issue of the decision to convey the Mall to the REIT, the facts actually negate any finding of malice. (See II.B., supra.)

4. The Effect of Fairfax's Conduct on the Smiths and Others

The Smiths argue (without any citation to the record) that the issues in this case have distressed them financially and emotionally, but they do not dispute that the results

[17] The Smiths again blur the distinction between Fairfax and John Price, who was not a party, and refer to "luxury" spending on an "executive jet" and the purchase of "art work" as somehow being relevant to the relative wealth analysis. Such focus is misguided because, as set forth above, the relevant inquiry is the relationship between Fairfax's total wealth and the size of the punitive damages award.

to them would have been at least equally disastrous if the Mall had been foreclosed upon. In trying to avoid foreclosure, Fairfax was attempting to benefit all partners, including the Smiths. Moreover, there is no evidence in the record that Fairfax's conduct affected any parties other than Fairfax and the Smiths, and as noted below, no other partners complained about the REIT. This factor does not justify an award of punitive damages that exceeds the 3:1 guideline.[18]

5. The Probability of Future Recurrences

Without any cited evidentiary basis or identification of other allegedly similar situations, the Smiths allege that "Price is and will be a recidivist unless punitive damages . . . are affirmed." (Smiths Br. at 43.) The Smiths' support for this assertion seems to be that Fairfax has never admitted wrongdoing. Such reasoning, however, would justify imposing punitive damages upon any party who actually defends an action brought against it. The situation here simply involves a valuation dispute in a one-time transaction between parties who will likely never have anything to do with each other

[18] The Smiths assert that the "investing public" was misled and injured by statements in the Prospectus that Price "own[ed]" the Mall and by the "backed-into" capitalization rate for the Mall. (Smiths' Br. at 43.) However, the Prospectus does not state that Price "owned" the Mall, but rather accurately states that the properties were "currently owned by privately organized partnerships" that would be contributed to the REIT "following completion of the offering." (P-71 at 1, 6, 14, 15, 23, 25, 44.) In addition, the Smiths offer no evidence that the Mall's capitalization rate (which was not disclosed in the Prospectus) was material to the "investing public." To the contrary, the evidence was undisputed that the investing public makes its decision based on the stream of income, so that the capitalization rate of a particular mall would not be relevant to their considerations—that is why REITs do not use appraisals. (R 4546 at 1293-95, 1305-06, 1328.) In any event, the REIT expert testified that the Mall's capitalization rate was set in accordance with commonly accepted REIT standards. (R 4546 at 1294.)

again. Moreover, no partner in any of the other thirty-eight partnerships that were involved with the REIT has made any kind of complaint or allegation of wrongdoing.[19] Nor is there any evidence in the record of any kind of wrongdoing on the part of Fairfax or John Price even in transactions unrelated to the Mall. There was no evidence of any pattern of wrongdoing, and the Smiths' answer of "who knows" (id. at 44) whether Fairfax has ever engaged in other similar conduct is insufficient as a matter of law.

6. The Relationship of the Parties

The Smiths argue that a large punitive damage award is appropriate because Fairfax was a fiduciary. However, as Fairfax previously explained, the relevant analysis turns on the specific facts of how that fiduciary relationship operated in this case. (Fairfax Br. at 42.) It is undisputed that this was a dispute between educated and experienced parties, and that Smith aggressively pursued his interest of obtaining a higher pay-off. Moreover, it was undisputed that Fairfax tried to provide relevant information (when permitted by law), and in fact favored the Smiths to its own disadvantage in the REIT. Fairfax's mistakes, if any, do not justify excessive punitive damages.

7. The Ratio of Punitive to Compensatory Damages

The Smiths argue that the ratio of punitive to compensatory damages in this case

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[19] The Smiths imply that one of Fairfax's representatives, Paul Mendenhall, scared or threatened a potential witness. (Smiths' Br. at 44.) In fact, Mr. Mendenhall merely told the witness that "the issue he was going to testify on had nothing to do with the REIT." (R 4542 at 534.) The trial court sustained an objection to Mr. Campbell's characterization of this comment as an effort to "intimidate" a witness. Id. In addition, there is no evidence as to why the Smiths' potential witness did not appear at trial.

was only 3.3 to 1 (if both prejudgment interest and attorneys fees are included in compensatory damages). (Smiths' Br. at 45.) The Smiths' argument that prejudgment interest and/or attorneys fees should be included in the calculation is not only unsupported, but contrary to Utah law on both points). See Amica Mut. Ins. Co. v. Schettler, 768 P.2d 950, 967 (Utah Ct. App. 1989) ("Attorneys fees are more properly considered costs and go on neither side of the scale when determining whether the amount of punitive damages awarded 'bear[s] a reasonable relation' to the amount of general damages"); First Sec. Bank v. J.B.J. Feedyards, 653 P.2d 591, 600 (Utah 1982) (prejudgment interest cannot be added to punitive damages); Seminole Pipeline Co., Mapco Inc. v. Broad Leaf Partners, 979 S.W.2d 730, 739 (Tex. Ct. App. 1998) (including interest in the ratio is equivalent to awarding interest on punitive damages). Consequently, when properly calculated, the ratio in this case is at least 13:1 and therefore presumptively excessive.[20]

The District Court failed to articulate why an award in excess of 3:1 was justified by reference to the Crookston I factors. A de novo examination of all of the facts in this case demonstrates that under the circumstances, this Court should totally eliminate or significantly reduce the punitive damages awarded in this case.

[20] Moreover, Fairfax told the Smiths in January 1994 that their REIT shares would be worth $230,000 (and Fairfax subsequently offered even more in March 1994). If the judgment is sustained, the Smiths must surrender their REIT shares, making the net value of their recovery approximately $180,000. Thus, the ratio of punitive damages to the true economic effect of the compensatory damages is over 30:1.

III. THE DISTRICT COURT ERRED IN ITS AWARD OF INTEREST.

A. The Smiths Are Not Entitled to "Interest" as Damages.

The jury awarded $690,000 in "interest" on compensatory damages of $410,000, which the District Court included in the Judgment. (Fairfax Br., tab A at 3-4, 5-6.) The Smiths do not dispute that they are not entitled to interest under Utah "prejudgment interest" rules, but they argue that "the time value of money [is] a substantive element of damages in a breach of fiduciary claim." (Smiths' Br. at 52; see also id. at 50 n.14.) However, Utah courts have evaluated interest in such cases under Utah's prejudgment interest rules and not as a component of damages. See, e.g., Lefavi v. Bertoch, 2000 UT App 5, ¶¶22-25, 994 P.2d 817.

The Smiths argue that other jurisdictions allegedly award interest as substantive damages for breach of fiduciary duty. (Smiths' Br. at 50-51.) However, the cited cases actually awarded interest under the applicable jurisdiction's "prejudgment interest" rules, which permit such interest in the fact finder's discretion.[21] (Fairfax Br. at 48 n.41 (quoting Wernick,[22] Ryan, Jefferson, Rolf, McDermott, Michelson).) See also Josephson

[21] The Smiths' reliance on "restitution" authorities (Restatement, Ryan, and Rosenthal) ignores that Utah rejects interest for equitable restitution. Bellon v. Malnar, 808 P.2d 1089, 1097 (Utah 1991); Dejavue, Inc. v. U.S. Energy Corp., 1999 UT App 355, ¶24, 993 P.2d 222.

[22] The Smiths quote the decision of the Illinois Court of Appeals rather than the Illinois Supreme Court. (Smiths' Br. at 50-51.) Although Fairfax discussed the higher court ruling in its initial brief, it is instructive to note that the Smiths eliminated from the lower appellate court decision the surrounding language inconsistent with their attempted distinction: "It is well-settled that *prejudgment interest* is a form of compensation, and that the decision whether to award *such interest* requires a balancing of the equities between the parties under the circumstances. . . . We therefore remand this cause with directions to award petitioners *prejudgment interest* at the prime rate."

v. Marshall, 2002 WL 1315604 at *4 (S.D.N.Y. June 17, 2002) ("prejudgment interest" awarded under New York statue in "action[s] . . . at law"); Spangler v. Jones, 861 S.W.2d 392, 397-99 (Tex. Ct. App. 1993) ("equitable prejudgment interest" permitted in trial court's "discretion" in Texas in broad range of cases). Unlike Utah, these jurisdictions merely employ discretionary and equitable prejudgment interest standards.

The Smiths ignore the seminal case of Fell v. Union Pacific Railway Co., 88 P. 1003 (Utah 1907), wherein this Court specifically criticized and rejected the Smiths' distinction (between prejudgment interest and damages) that would "allow interest or not, as in [the jury's] judgment may seem proper, as a part of the damages." Id. at 1006. This Court explained that a "fixed rule" is "a safer guide than the judgment of a few individuals," whether the "court or jury," because any other rule "must lead to uncertainty, and may tend to favoritism in its application." Id. The policies of full compensation and deterrence (advanced by the Smiths in favor of its distinction) have already been taken into account in the formulation of Utah's existing prejudgment interest rules. Trail Mountain Coal Co. v. Utah Division of State Lands and Forestry, 921 P.2d 1365, 1370 (Utah 1996). This Court should follow existing law and deny discretionary, equitable prejudgment interest in this case.

B. The Jury's Award of Interest Was Clearly Excessive.

The benefit of Utah's prejudgment interest rules is illustrated by the jury's award of interest in this case, which exceeded by $92,779 the compounded interest figure put in

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Estate of Wernick, 502 N.E.2d 1146, 1154 (Ill. Ct. App. 1986), aff'd in part, rev'd in part, 535 N.E.2d 876, 888 (Ill. 1989).

evidence by the Smiths at trial. (Smiths' Br. at 53.) No one knows how the jury reached that figure, but the Smiths now speculate that the jury was awarding interest on its $30,000 water contribution. The Smiths make no attempt to demonstrate or defend how the jury could have permissibly calculated that amount of interest on the water rights.[23] In any event, as a matter of law, contributions to capital accounts, such as these water rights (as opposed to capital calls), do not bear interest. (P-15 art. 4 ("No interest shall be payable on any contributions to the capital of the Partnership"); P-45 (water rights transferred in "consideration of a $30,000 increase in my capital account"). Consequently, the jury's damage award was clearly excessive and must be reduced. The excessive interest, just as the excessive punitive damages, demonstrates that the jury was motivated by passion or prejudice in this case.

CONCLUSION

The judgment should be reversed and this case should be remanded for entry of judgment n.o.v. on (1) all claims because the REIT was the only alternative to save the Mall, (2) all punitive damages claims because of the failure to establish willful misconduct, and/or (3) all claims for interest. Alternatively, this Court should reduce the punitive damages award to an appropriate amount or remand for a new trial.

[23] The only evidence at trial was that the compounded interest rate used by the Smiths was roughly the same as 10 percent simple interest. (R 4542 at 2163.) Consequently, ten years of interest on $30,000 would be merely one third of the excess interest award.

DATED this 15th day of November, 2002.

RAY, QUINNEY & NEBEKER

James S. Jardine
Attorneys for Appellants

CERTIFICATE OF SERVICE

THIS IS TO CERTIFY that on the 15th day of November, 2002, two true and correct copies of the REPLY BRIEF OF APPELLANTS were hand-delivered to:

Mr. Robert S. Campbell, Jr., Esquire
Van Cott, Bagley, Cornwall & McCarthy
50 South Main, Suite 1600
Post Office Box 45340
Salt Lake City, Utah 84145-5340
Attorneys for Appellees

676094 03